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Supreme Court of the United States

October Term, 1969

No. 1103

AMERICAN STEAMSHIP OWNERS MUTUAL PROTECTION AND INDEMNITY ASSOCIATION, INC.,

Petitioner,

—against—

ARTHUR L. LIMAN, As Trustee in Bankruptcy of A. H. BULL STEAMSHIP CO.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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ARTHUR L. LIMAN, As Trustee in Bankruptcy of A. H. BULL STEAMSHIP CO.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner prays that a writ of certiorari issue to review a final judgment of the United States Court of Appeals for the Second Circuit entered on October 24, 1969, which affirmed a declaratory judgment in favor of the respondent (trustee in bankruptcy of a steamship company hereinafter referred to as the "Trustee") declaring that the petitioner (hereinafter sometimes referred to as the "indemnity insurer") will be obligated to indemnify the Trustee on the basis of gross payments he purportedly makes under his proposed plan, the effect of which requires seamen and longshore personal injury claimants to turn back to the Trustee a portion of each judgment paid and to remain general creditors of the estate to that extent, in order for the Trustee to avoid compliance in fact with the deductible payment provision of the indemnity insurance contracts.

Opinions Below

The opinion of the District Court (Walter R. Mansfield, District Judge) and the memorandum opinion of the Court of Appeals are appended hereto. The District Court's opinion, dated March 4, 1969, is reported at 299 F. Supp. 106. The opinion of the Court of Appeals which adopts the District Court's opinion is reported at 417 F. 2d 627.

Jurisdiction

The jurisdiction of this court to review the judgment of the United States Court of Appeals for the Second Circuit is invoked under 28 United States Code, §1254 (1).

Questions Presented

1. Whether the declaratory judgment requiring the marine indemnity insurer to indemnify the Trustee in bankruptcy, pursuant to a plan of the Trustee (in purported compliance with the deductible payment provision of the insurance contracts) obligating seamen and longshore personal injury claimants to turn back to the Trustee a sum equal to the deductible, gives the Trustee rights not available to the bankrupt under the original contract, violates §70(a) of the Bankruptcy Act and constitutes an inequitable and improper exercise of judicial power under the Bankruptcy Act?

2. Whether the declaratory judgment authorizing the Trustee's shifting the estate's share of defense costs, under a marine indemnity insurance policy, to seamen and longshore personal injury claimants (by the Trustee's exacting from claimants, in advance of his undertaking the defense of each lawsuit, an agreement that should the claimant

recover judgment the Trustee will satisfy it only upon claimant's repaying to the estate the defense costs recoverable under the policies) violates §64 of the Bankruptcy Act and constitutes an inequitable and improper exercise of judicial power under the Bankruptcy Act?

Statutes Involved

The pertinent provisions of §70 (a) of the Bankruptcy Act (11 USC §110):

§ 70. Title to property

(a) The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this Act, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located

* * *

(5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred

* * *

(6) rights of action arising upon contracts

* * *

The pertinent provisions of §64 of the Bankruptcy Act (11 USC §104):

§ 64. Debts which have priority

(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment,

shall be (1) the costs and expenses of administration, including the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition

* * *

The pertinent provisions of the New York Insurance Law (27 McKinney's Consolidated Laws):

Subsection 2 of Section 167. No policy or contract insuring liability to person * * * shall be issued or delivered in this state, unless it contains in substance * * *:

(a) A provision that the insolvency or bankruptcy of the person insured, or the insolvency of his estate shall not release the insurer from the payment of damages for injury sustained or loss occasioned during the life of and within the coverage of such policy or contract.

(b) A provision that in case judgment against the insured or his personal representative in an action brought to recover damages for injury sustained or loss or damage occasioned during the life of the policy or contract, shall remain unsatisfied at the expiration of thirty days from the serving of notice of entry of judgment upon the attorney for the insured, or upon the insured, and upon the insurer, then an action may, except during a stay or limited stay of execution against the insured on such judgment, be maintained against the insurer under the terms of the policy or contract for the amount of such judgment not exceeding the amount of the applicable limit of coverage under such policy or contract.

Subsection 4 of Section 167. The provisions of this section shall not apply * * * to the kinds of insurance

set forth in paragraph (c) of subsection two of section one hundred twelve.

The insurance set forth in paragraph (c) of subsection 2 of Section 112 is

> * * * (c) marine insurance of the following kind or kinds * * * (2) Insurance in connection with ocean going vessels against any risk specified in paragraph twenty-one of section forty-six.

In turn, the risks specified in Subsection 21 of Section 46 (referred to in Subsection 2 of Section 112) are

> 21. Marine protection and indemnity insurance, meaning insurance against, or against legal liability of the insured for, loss, damage or expense arising out of, or incident to, the ownership, operation, chartering, maintenance, use, repair or construction of any vessel, craft or instrumentality in use in ocean or inland waterways, including liability of the insured for personal injury, illness or death or for loss of or damage to the property or another person.

Statement

This declaratory judgment action was commenced by the Trustee in bankruptcy of A. H. Bull Steamship Co. in the United States District Court for the Southern District of New York under the court's ancillary bankruptcy jurisdiction wherein he put forth a number of plans which he submitted would constitute payment under the bankrupt's contracts of marine indemnity insurance (R1).*

---

* R refers to the pages of the certified record and A refers to the Appendix to this petition.

A. H. Bull Steamship Company was insured under marine indemnity insurance contracts, each of which contained the following relevant provisions:

"The Association agrees to indemnify the Assured against any loss, damage or expense which the Assured shall become liable *to pay and shall pay* by reason of the fact that the Assured is the owner * * * of the insured vessel which shall result from * * *:

(1) Liability for life salvage, loss of life of, or personal injury to, or illness of, any person, * * *

(e) Claims hereunder, * * * are subject to a *deduction of $1,000.00* with respect to each accident or occurrence." (Emphasis supplied)

* * *

"(13) Liability for costs, charges and expenses reasonably incurred *and paid by the assured* in connection with any liability insured under this policy, subject however, to the *same deduction* that would be applicable under this policy to the liability defended * * *." (Emphasis supplied)

(a) It is understood and agreed that the Association may undertake the investigation of any occurrence which might develop into a claim against the Assured, and may undertake the investigation and defense of any claim made against the Assured with respect to which the Assured shall be or may claim to be insured by the Association, and that during such investigation and/or defense the Association may incur expenses, which expenses shall be for the account of the Assured

* * *

The opinion of District Judge Mansfield (A 5a) notes that the bankrupt had agreed to be indemnified by the indemnity insurer, "as the owner, charterer or operator of

certain vessels, including losses sustained as a result of personal injury claims, subject to a deductible of $1,000" on each claim, and that the claims in question were "by seamen and longshoremen for personal injuries, of which approximately 120 suits involving 114 accidents or occurrences fall within the coverage of the policies."

There is no controversy whatsoever that the policies in dispute are marine indemnity for payment policies under which the petitioner's liability to the insured specifically arises only after the insured has actually paid a loss.

The Trustee's motion (R12) for summary judgment (granted by the District Court and sustained by the Court of Appeals) presented the specific plan described to some extent in the District Court's opinion (A 5a).

Briefly stated, under the Trustee's plan, he would seek to meet the deductible provision without diminishing the estate of the bankrupt in any manner and collecting the full amount of the actual out of pocket payment from the petitioner. Thus, each personal injury claimant before collecting the proceeds of a judgment would first have to agree to turn back the amount of the deductible to the Trustee. He would retain his status of a general unsecured creditor as to this amount returned, with virtually no chance of recovering any part thereof from the estate. Indeed, the complaint states at paragraph 16 "it presently appears unlikely that general creditors will receive any payment on the liquidation under the reorganization of the debtor." The Trustee, under the plan, as approved, would then compel the indemnity insurer to reimburse him for the sum actually retained by the claimant over the deductible even though the deductible has remained in fact unpaid by the estate. Consequently, the Trustee has effectively deleted the deductible provision from the indemnity contract notwithstanding that the premium was based upon the deductible.

As can be seen from the foregoing the Trustee's plan, as approved, sanctions the Trustee's satisfying his self-insured interest imposed by the deductible at the expense of the injured longshoremen or seamen and allows him to obtain the full benefit of the indemnity policies without meeting the deductible requirement and without having paid the requisite premium for non-deductible insurance contracts.

The Court of Appeals, in its memorandum opinion (A 1a) construed the declaratory judgment to hold that the indemnity insurer "is obligated to indemnify the Trustee for the payment of personal injury claims within the scope of the policies" and that they "contain a $1,000 deductible and the Trustee has arranged that upon his payment of a judgment against the estate the claimant will repay $1,000 and become a general creditor for that amount", without recognizing that the turning back by the claimant of that sum hardly constitutes a payment, since the arrangement is a mere charade, whereby the claimants turn back the $1,000 to the Trustee as a condition of the satisfaction of each claim and that the claimants, by reason of this species of a "kickback", are, in fact, never paid that sum at all.

The District Court's opinion does not urge that the estate lacks funds to lay out for the defense or actual payment of the sum of $1,000 for each claim (characterized as a "relatively few thousand dollars" [A 8a] to enforce the bankrupt's indemnity insurance assets insuring "many thousands of dollars" [A 7a, 8a]). Instead, the opinion urges that the reason why the Trustee may refrain from real compliance with the deductible requirement of the indemnity insurance contracts is that the Government, as a priority creditor, opposes the hiring of special counsel to defend the claimants' law suits or to actually pay the claims to the extent

of such $1,000, although retention of special counsel to defend certain personal injury actions had been authorized in the past. By the insistence that such true payments would diminish the estate available for its claims, despite the fact that such payments would be administrative expenses under Section 64 of the Bankruptcy Act needed to preserve the bankrupt's rights under its indemnity insurance contracts as property of the estate, a priority creditor could obtain immunity from expenditures to which all creditors of the estate are subject, a privilege to which it is not entitled to by the Bankruptcy Act or by any other law.

Although Judge Mansfield further stated that "this position was upheld by the Hon. Edward J. Ryan, Referee in Bankruptcy, acting as Special Master," this is incorrect, since the Referee never passed on that question but merely denied the motion for appointment of special counsel, at that time, "without prejudice to renewal" as shown by his report annexed as an appendix to this Petition (A 15a). The opinion of the District Court notes that the Trustee acknowledges that under the deductible clause the Trustee's right to indemnity "depends upon a showing that the estate has made payment to the third party claimant of the amount for which reimbursement is sought from defendant." Consequently, there is no doubt that Judge Mansfield's opinion requires payment by the Trustee of the $1,000 deductible (even if feigned, apparently) before any resort to the indemnity insurance contract could be had.

The opinion falls into the error of confusing the contractual issue in this case with the issues involved in cases arising from provisions of New York insurance contracts indemnifying for "loss" rather than for actual payment and which are not ocean marine contracts, relying on those cases as embodying the New York decisional law. Moreover, none of the cases has anything to do with the question

of whether a purported payment to a claimant who must agree to turn back a portion of the payment as a firm condition for receiving a satisfaction of his claim is an actual payment under the "shall pay" provision of an indemnity insurance policy. The court's attempt to equate this transparent metaphysical exercise with the payment to a claimant by a third party on behalf of an insured's obligation is without any legal or factual support, since a claimant paid through a third party is actually made whole and the real recipient of such payment.

On the other hand, the District Judge concedes that the "policy thus expressed in New York decisional law" is one which "stands upon a separate footing from that declared by the Legislature in New York's Insurance Law" which declared "inapplicable to marine insurance against personal injury," the requirement that insolvency or bankruptcy of the insured shall not release the insurer from its obligation to indemnify.

Reasons For Granting the Writ

I

The decisions below raise important questions in the administration and application of the Bankruptcy Act to the shipping industry, particularly with respect to indemnity insurance contracts for personal injury claims of maritime workers, the application of § 70(a) and § 64 of that Act to the deductible self-insurance provisions of such contracts, and the enforcement of such contracts as assets of the bankrupt's estate.

Section 70 of the Bankruptcy Act gives to the Trustee in bankruptcy the title to the property held by the bankrupt. However, "the Trustee succeeds *only to such rights as the bankrupt possessed*; and the Trustee is subject to all

claims and defenses which might have been asserted against the bankrupt but for the filing of the petition." (Emphasis supplied) *Bank of Marin* v. *England,* 385 U.S. 99, 101 (1966) The same principle was expressed in *Zartman* v. *First National Bank*, 216 U.S. 134 (1910), when the court stated at page 138:

> "* * * The Trustee claims that he takes the same kind of title as a *bona fide* purchaser for value, but the rule applicable to this and all similar cases is that the Trustee takes the property of the bankrupt, not as an innocent purchaser, but as the debtor had it at the time of the petition, subject to all valid claims, liens and equities. *Thompson* v. *Fairbanks*, 196 U.S. 516, and cases cited. And this is so well settled that our jurisdiction of the writ of error is exceedingly doubtful." * * *

Since the indemnity insurance contract required a $1,000 *payment* by the bankrupt the same requirement would hold true for the Trustee. Consequently, the courts below have exceeded their power by deleting from the indemnity insurance contract the deductible payment provisions and substituting a right accorded the Trustee which was neither contained in the insurance contract nor imposed by section 167 of the New York insurance law, which exempts marine insurance from its bankruptcy clause requirements.

Turning to the question of the type of expense involved, clearly this $1,000 deductible would fall within § 64 of the Bankruptcy Act as a cost and expense of administration and preservation of the estate. As the Trustee's affidavit in support of the motion urged, "the insurance policies here involved are an asset of the estate." Furthermore, by provision of the contract the expenses incurred in defense of the longshoremen and seamen's claims, such as legal fees, are subject to the same deductible provision.

These costs would in all the usual cases and in especially litigated cases exceed the $1,000 deductible, yet the Trustee is unwilling to pay such expenses unless the bankrupt had already used up the deductible expenses paid prior to bankruptcy. It appears that there would be ample funds in the estate to pay these administration costs, but of course, this would diminish the general assets of the estate, as any administrative cost does, and thereby reduce the amount of money available to the government as a priority creditor. This, though, should not be an objection, as the expenses so incurred will be to preserve the greater assets of the estate and are specifically envisoned in the Bankruptcy Act at § 64.

II

The past history of maritime personal injury litigation reveals that the concepts of liability under federal law have been constantly expanding. *Seas Shipping Co.* v. *Sieracki*, 328 U.S. 85 (1946) and *Mascuilli* v. *United States*, 387 U.S. 237 (1967). The insurance held by the shipowners and its place in bankruptcy, therefore, has great importance, and since the greatest portion of insurance held by shipowners is indemnity for payment insurance, we respectfully submit that the questions arising from the decision below should be determined by this Court.

III

Although this court has expressed its concern for the rights of maritime workers for personal injuries sustained while in the pursuit of their vocation, it has not determined the rights of such workers for personal injuries against bankrupt shipowners under the prevailing indemnity insurance contracts concerning their claims in bankruptcy in relation to priority creditors' claims.

The Federal courts have long held that seamen are the wards of admiralty and as such have sought to protect them. *Garrett* v. *Moore-McCormack Co.*, 317 U.S. 239 (1942). Longshoremen and other maritime workers have received similar consideration. *Seas Shipping Co.* v. *Sieracki*, 328 U.S. 85 (1946).

The approval by the courts below of the transparent subterfuge devised to avoid the contractual obligations of the parties to the indemnity insurance contract and to force the maritime worker to turn back a portion of his recovery is highly inequitable to both the maritime worker and indemnity insurer. As this court stated in *Bank of Marin* v. *England*, *supra*, 385 U.S. 99, 103 (1966), "There is an overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction."

IV

The Court of Appeals in adopting the opinion of the District Court, decided an important question of state insurance law in conflict with the law of the state as expressed in the New York Insurance Law, which specifically provides that the provisions that insurers are not released by the insureds' bankruptcy, and for direct suit against the insurers after judgment, are required to be included in contracts of insurance are not applicable to marine protection and indemnity insurance.

Section 167 of the New York Insurance Law mandates certain provisions to be part of every insurance contract. Sections 167 1 (a) and 1 (b) require the inclusion of clauses that the insolvency or bankruptcy of the person insured will not release the insurer from the payment of damages and for a direct suit against the insurer.

Although Section 167 was at one time held applicable to marine policies of indemnity (*Hansen* v. *Continental Insur-*

ance Co., 262 N.Y. 136 (1933)), this was changed by the New York Legislature in a statutory amendment passed in 1940 (Chapter 507 of The Laws of New York, 163rd Session, 1940) to Sub-section 4 of Section 167 which provides as follows:

> "The provisions of this section shall not apply to any contract of insurance in so far as it covers the liability of an employer for workmen's compensation, * * * nor to the kinds of insurance set forth in paragraph (c) of sub-section two of section one hundred twelve."

The insurance set forth in paragraph (c) of Sub-section 2 of Section 112 of the New York Insurance Law is:

> "* * * (c) Marine Insurance of the following kind or kinds * * * (2) Insurance in connection with ocean going vessels against any risk specified in paragraph twenty-one of section forty-six."

In turn, the risks specified in Sub-section 21 of Section 46 of the New York Insurance Law (referred to in Subsection 2 of Section 112) are:

> "21. 'Marine protection and indemnity insurance,' meaning insurance against, or against legal liability of the insured for, loss, damage, or expense arising out of, or incident to, the ownership, operation, chartering, maintenance, use, repair or construction of any vessel, craft or instrumentality used in ocean or inland waterways, including liability of the insured for personal injury, illness or death or for loss of or damage to the property of another person."

Thus, is it readily apparent that the law of New York, as expressed by its statutes, has removed marine insurance from its purview. As previously stated, the District

Judge noted that the "policy" he acknowledged was "declared by the Legislature" as being different from the "policy" he reasoned as having been "expressed in New York decisional law". Yet the "decisional law" he cited as expressing that "policy" involved neither "shall pay" indemnity insurance contracts nor marine insurance policies excepted from § 167. Clearly, the courts below disregarded this statutory distinction when referring to the decisional "policy" of New York expressed only in unrelated insurance contract decisions. Indeed, the decisional law as expressed in *Meridian Trading* v. *National Automobile and Casualty Co.*, 45 Misc. 2d 847 (Sup. N.Y. 1964) at page 849, recognizes the statutory distinction which "excludes marine protection and indemnity policies from its scope [the requirements of § 167]".

CONCLUSION

The petition for writ of certiorari should be granted, and thereupon the decision of the United States Court of Appeals should be reversed.

Dated: January 20, 1970.

Respectfully submitted,

LOUIS J. GUSMANO
Counsel for Petitioner

DANIEL J. DOUGHERTY
ROBERT C. MIRONE
CHARLES N. FIDDLER
of Counsel

Opinion of Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 156—September Term, 1969.

(Argued October 15, 1969 Decided October 24, 1969.)

Docket No. 33605

ARTHUR L. LIMAN, as Trustee in Bankruptcy of A. H. BULL STEAMSHIP CO.,

Plaintiff-Appellee,

—against—

AMERICAN STEAMSHIP OWNERS MUTUAL PROTECTION AND INDEMNITY ASSOCIATION, INC.,

Defendant-Appellant.

Before:

FRIENDLY, HAYS and ANDERSON,

Circuit Judges.

Appeal from a judgment of the District Court for the Southern District of New York, Walter R. Mansfield, *Judge,* granting the motion of the trustee in bankruptcy of a steamship company for a declaration that its indemnity insurer is obligated to indemnify it for the payment of personal injury claims covered by its policies. Affirmed.

AMBROSE DOSKOW (Rosenman, Colin, Kaye, Pteschek, Freund & Emil, Peter F. Nadel, of Counsel), *for Plaintiff-Appellee.*

Opinion of Court of Appeals

LOUIS J. GUSMANO (Kirlin, Campbell & Keating, of Counsel), *for Defendant-Appellant.*

PER CURIAM:

The issue on this appeal from a judgment of the District Court for the Southern District of New York is whether the court properly granted a declaratory judgment that the indemnity insurer of A. H. Bull Steamship Company, now in bankruptcy in that court, is obligated to indemnify the Trustee for the payment of personal injury claims within the scope of the policies. These contain a $1,000 deductible and the Trustee has arranged that upon his payment of a judgment against the estate the claimant will repay $1,000 and become a general creditor for that amount. The insurer argues that all the insured is paying is the net amount plus its expenses and that it is entitled to deduct $1,000 from that sum rather than from the gross recovery and expenses. Judge Mansfield, in a well-considered opinion, held the contrary. We agree and can find nothing to add.

Judgment affirmed.

Judgment of Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-fourth day of October, one thousand nine hundred and sixty-nine.

PRESENT:

HON. HENRY J. FRIENDLY,
HON. PAUL R. HAYS,
HON. ROBERT P. ANDERSON,
Circuit Judges.

ARTHUR L. LIMAN, Trustee in Bankruptcy of
A. H. Bull Steamship Co.,

Plaintiff-Appellee,

v.

AMERICAN STEAMSHIP OWNERS MUTUAL PROTECTION AND INDEMNITY ASSOCIATION, INC.,

Defendant-Appellant.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

Judgment of Court of Appeals

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed with costs to be taxed against the appellant.

A. Daniel Fusaro
Clerk

Opinion of Mansfield, *D.J.*

In the declaratory judgment action plaintiff, as Trustee in Bankruptcy of A. H. Bull Steamship Company ("Bull"), moves pursuant to Rule 56, F.R.C.P., for summary judgment declaring the Trustee's right to reimburse under certain insurance polices issued by defendant. For the reasons indicated below, the motion is granted. The undisputed facts are as follows:

Bull, which was engaged in the business of operating merchant vessels before it went into bankruptcy, is the assured in certain indemnity insurance policies issued by defendant, for which Bull paid premiums in excess of $300,000 annually. Under the terms of the policies defendant, as insurer, agreed to indemnify Bull against loss, damages and expenses sustained by it as the owner, charterer or operator of certain vessels, including losses sustained as the result of personal injury claims, subject to a deductible of $1,000. Following a Chapter X Reorganization proceeding Bull was adjudicated a bankrupt and plaintiff was appointed its Trustee in Bankruptcy. In the meantime various actions have been instituted against Bull or its Chapter X Trustee by seamen and longshoremen for personal injures, of which approximately 120 suits involving 114 accidents or occurrences fall within the coverage of the policies. Defendant has the right to assume the defense of the actions but is not obligated to do so. Following its refusal to do so, the Chapter X Trustee sought authority to retain special counsel to defend certain of the lawsuits. Thereupon the Government, a large priority creditor, opposed on the grounds that the estate would be diminished to the extent of the $1,000 deductible which would be attributed to each of the claims to be defended and that the expenditure of such sums by the Trustee would violate the Government's priority in the distribution of the assets of the estate. This positon was upheld by the Hon.

Edward J. Ryan, Refree in Bankruptcy, acting as Special Master.

Following defendant's refusal to take over the defense of the actions or to reimburse plaintiff unless it first satisfied the judgments or settlements in full, including payment of the $1,000 deductible (for which the debtor would not be entitled to reimbursement from defendant), the Chapter X Trustee brought the present action for declaratory judgment to the effect that the $1,000 deductible requirement might be satisfied in one of several different ways, but pointed out that the Trustee could not implement any of its proposals without court approval and assurance of reimbursement from defendant because the $1,000 payments, as pointed out by the Government and Special Master, would deplete the estate and amount to a preference over other general creditors in violation of the Bankruptcy Act.

The stumbling block giving rise to the present controversy is found in the following provision of the insurance policies issued by defendant to Bull:

> "The Association agrees to indemnify the Assured against any loss, damage or expense which the Assured shall become liable to pay and shall pay by reason of the fact that the Assured is the owner . . . of the insured vessel and which shall result from . . . :
>
> "(1) Liability for life salvage, loss of life of or personal injury to, or illness of, any person. . . .
>
> "(e) Claims hereunder, . . . are subject to a deduction of $1,000 with respect to each accident or occurrence."

Plaintiff acknowledges that under the above-quoted clause the estate's right to indemnity for any loss sustained by it

on account of an accident or occurrence covered by the policies, after deduction of $1,000, depends upon a showing that the estate has made payment to the third party claimant of the amount for which reimbursement is sought from defendant. For example, upon satisfaction of a $10,000 judgment against the estate, plaintiff would be entitled to $9,000 from defendant, i.e., the $10,000 paid out by the estate, less the $1,000 deductible. The Trustee, however, cannot permit the claimant to retain the $1,000 not covered by the indemnity policy, since the $1,000 would then, because of the estate's insolvency, amount to an illegal preference. The Trustee therefore proposes to finance the $1,000 deductible in each case by defending each lawsuit pursuant to an agreement with the claimant to the effect that in the event of recovery or settlement in an amount in excess of $1,000, the estate will pay the full amount of the recovery to the claimant and the claimant will thereupon repay $1,000 to the estate, in exchange for which the claimant will become a general creditor of the estate in the sum of $1,000. The United States has by affidavit stated that it has no objection to the proposed plan, since there would be no invasion of the priority rights of the United States, as a creditor in the bankrupt estate.

It is plaintiff's position that the source of the funds used to finance the $1,000 deductible is of no concern to defendant and should not affect defendant's obligation to reimburse the estate for any bona fide payments made to claimants on account of their personal injury claims covered by the policies. Defendant, on the other hand, contends that in order to be indemnified under the policies the estate must show that it actually "absorbed" the $1,000 deductible. The effect of defendant's position, it seems to be conceded, would be to enable it to escape payment of judgments possibly running into many thousands

of dollars solely because the estate, due to its insolvency, is unable to pay out of its own funds the relatively few thousand dollars required to satisfy defendant's concept that the assured must "absorb" the deductible. It is in this context that the Trustee seeks summary judgment pursuant to Rule 56, F.R.C.P., declaring that the procedure proposed by it, if carried out by the estate, will obligate defendant to reimburse the estate in the amount of the claims paid, less $1,000.

Since the undisputed facts reveal a substantial controversy with respect to adverse legal interests necessitating a determination as to the rights of the parties, the subject matter is appropriate for resolution by way of declaratory judgment. See *Maryland Casualty Co.* v. *Pacific Co.*, 312 U.S. 270 (1941). It is equally clear that in the absence of any specific provision of maritime law governing the issue here presented, see *Kossick* v. *United Fruit Co.*, 365 U.S. 731, 742 (1960)[1]—and we know of none—regulation of such marine insurance contracts is controlled by state rather than federal law. *Wilburn Ins. Co.* v. *Fireman's Ins. Co.*, 348 U.S. 310 (1954). As defendant is a New York corporation, Bull had its principal place of business in New York and the only proof submitted indicates that the policies were delivered to Bull in New York, New York law should serve as the principal guide to the construction of this contract.

New York's policy in construing provisions of insurance contracts dealing with the insurer's obligation to indemnify against loss was summed up in a recent decision, *Henegan* v. *Merchants Mutual Insurance Co.*, App. Div. 2d (1st Dept., Nov. 7, 1968), where the court, rejecting an insurer's contention that it was not required to make payments to the insured for the reason that the latter had failed to pay excess judgments over the policy limits, stated:

> "To hold that prior payment must be shown before action by the insured, would permit the insurer to take advantage of the financial status of its insured and deprive the ultimate beneficiary claimant of his judgment. Such a holding would be contrary to the purpose and spirit of our law." Cf. *Meridan Trading* v. *Nat Auto Ins.*, 45 Misc. 2d 847, 850-51 (Sup. Ct. 1964).

Guided by this fundamental standard of fairness and equity, the courts of New York have repeatedly held that an insured fulfills his obligations under an indemnity policy and is entitled to reimbursement when a judgment against him has been satisfied, and the insurer may not escape its obligation to indemnify by showing that the payment made by the assured was advanced to it by a third party or financed in some other fashion. *Employers Liability Assurance Corporation, Ltd.* v. *International Milk Products Co.*, 192 App. Div. 88 (1st Dept. 1920); *Campbell* v. *London & Lancashire Ind. Co. of America*, 168 N.Y. Supp. 300 (Sup. Ct. Erie Co. 1917).

> "The contention that the policy is one of indemnity with respect to damages and not for liability merely is sound, but I am unable to agree with the contention that it was essential to a right of action in the plaintiff by subrogation that the payment should have been made by the Shattuck Company from its own funds. . . . It was at liberty, so far as the defendant is concerned, to borrow the money and pay the judgment even though it was insolvent or on the verge of insolvency. It was not essential that the judgments should be paid by its own funds. It is quite sufficient if they were paid for it, either by a loan or a gift of the money to it for that purpose or at its request, by whch it would incur an independ-

> ent liability for reimbursement. In either instance, it would be entitled to recover over against defendant and it would incur a *loss* within the terms of the policy by the payment of the judgments." (192 App. Div. at 91-92)

While the above decisions do not deal with the precise type of condition precedent to indemnity claimed here, they make it clear that the test in New York is whether the assured has actually in good faith sustained the loss for which reimbursement is sought, and the insurer's obligation to indemnify may not be avoided because of the assured's insolvency.[1]

Applying those principles here, there is no doubt amout the fact that under his proposal the Trustee would be seeking reimbursement only for losses actually sustained by the estate, without any resulting benefit accruing to it, and there is no evidence that the Trustee would be acting in bad faith in defending the pending lawsuits and paying any judgments obtained by the claimants against the estate. If defendant, on the other hand, were permitted to avoid making reimbursement simply on the ground that the Trustee had not ultimately paid the $1,000 deductible out of its own pocket, the result would indeed be to "permit the insurer to take advantage of the financial status of its insured and deprive the ultimate beneficiary claimant of his judgment." *Henegan* v. *Merchants Mutual Insurance Co., supra.* Here the ultimate beneficiaries are those personal injury claimants who have suffered losses because of Bull's negligence or the unseaworthiness of its ships. Defendant was paid very substantial premiums, more than $300,000 annually, to enable Bull to pay such claims. Yet, under its construction of the policy, it would in effect reap a windfall at the expense of the intended beneficiaries. Such a result "would be contrary to the purpose and spirit" of New York law.

No purpose, expressed or implied, in the insurance policies in this case would be served by the condition precedent proposed by defendants to the effect that the $1,000 deductible must be "absorbed" by the estate. The purpose of such a deductible is not to assure that payment will be made only to solvent policy holders. Its primary purpose is to enable the insurer to avoid responsibility for small claims which are usually both numerous and costly. That purpose is fully served by the Trustee's proposal. The source of the $1,000 deductible should be of no concern to the defendant, since it is not required to reimburse the estate for losses under $1,000 suffered by the claimants. Furthermore, it is adequately protected against unjustified settlements or negligent defenses on the part of the Trustee; under the terms of the policy defendant has the right to assume the defense of any action and the assured must aid in such defense. In addition defendant is further protected by provisions to the effect that it need not indemnify the estate for unreasonable expenses incurred in the defense of an action or for settlements in excess of the amount authorized by defendant. Thus the defendant under the proposal made by the Trustee gets the full benefit of its bargain and does not relinquish any rights under its contracts. It is not, however, entitled to the windfall sought by it at the expense of the ultimate beneficiaries of the policies.

The situation here differs in significant legal and practical respect from that found in decisons cited by the defendant, where recovery was denied because there was neither a bona fide settlement of the judgment obtained by the claimant against the assured nor a payment made by the assured of the amount for which reimbursement was claimed. *Stenbom* v. *Brown-Corliss*, 137 Wis. 564, 119 N.W. 308 (1909); *Eberlein* v. *Fidelity & Deposit Co.*, 164 Wis. 242, 159 N.W. 553 (1916). Here the Trustee would satisfy each judgment against the estate and ac-

tually pay out of the estate to the claimant all funds for which reimbursement will be sought from defendant. Under the Trustee's proposed plan it is true that the estate will receive $1,000 back from each claimant. Since the estate is bankrupt, however, and the claimant becomes a creditor against it in the identical amount of $1,000, no benefit results to the assured. In any event, the effect of the arrangement is to impose upon the insurer the obligation to reimburse losses in excess of the deductible which was the bargain defendant undertook. Such an arrangement can hardly be characterized as one made in bad faith and it differs sharply and materially from one where the assured shares, for its own benefit, monies which the insurer is obligated to pay only as reimbursement of losses sustained by the claimant. Here the assured gets no such benefit.

For the foregoing reasons the Court grants plaintiff's motion for summary judgment declaring that defendant will be obligated to indemnify plaintiff for payments made in accordance with the Trustee's proposed plan.

Settle order on notice.

Dated: March 4, 1969.

WALTER R. MANSFIELD
U.S.D.J.

FOOTNOTES

[1] The policy thus expressed in New York decisional law stands upon a separate footing from that declared by the Legislature in New York's Insurance Law §167(1)(a), which provides that the insolvency or bankruptcy of the insured shall not release the insurer from its obligation to indemnify. The section was made inapplicable to marine insurance against personal injury, §§46(21), 112(c)(1), perhaps because of the controversy with respect to applicability of state direct action statutes to maritime law.

Declaratory Judgment

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

Plaintiff having moved by notice of motion dated October 11, 1968 for summary judgment declaring that defendant will be obligated to indemnify plaintiff under the policy annexed to the complaint herein, and similar policies, for payments made on account of any judgment or settlement of an action brought against the insured which is within the coverage of such policy notwithstanding the fact that the claimant who shall have received such payment shall have agreed in advance to pay to plaintiff the deductible amount under such policy.

Now on the complaint and answer and all prior proceedings herein, the notice of motion dated October 11, 1968, the affidavits of Arthur L. Liman, sworn to October 11, 1968 and November 18, 1968, and the affidavit of Irwin B. Robins, sworn to October 11, 1968, and said motion having duly come on for argument, and due deliberation having been had, and the Court having filed its opinion on March 5, 1969, it is

ORDERED, ADJUDGED AND DECREED that said motion of plaintiff be and it hereby is in all respects granted, and that the rights and obligations of the parties hereto with respect to the issue framed by the pleadings herein be and they hereby are determined as follows:

> Upon payment by plaintiff of any judgment in, or amount agreed upon in settlement of, any action

arising out of an accident or occurrence within the coverage of the insurance policy annexed to the complaint herein as Exhibit A thereto or any similarly worded policy, plaintiff shall be entitled to be indemnified by defendant in accordance with the terms of such policy notwithstanding the fact that the claimant who shall have received such payment shall have agreed in advance to pay to plaintiff an amount equal to the deduction from defendant's indemnity obligation thereunder or such portion thereof as shall not theretofore have been expended by the insured.

Dated: New York, New York
March 12, 1969

WALTER R. MANSFIELD
U.S.D.J.

Referee Ryan's Report

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

In the Matter

of

SEATRADE CORPORATION, et al.,

Debtor.

In Proceedings Under Chapter X of the Bankruptcy Act

No. 63 B 216

REFEREE'S REPORT ON APPLICATION FOR AN ORDER AUTHORIZING THE APPOINTMENT OF SPECIAL COUNSEL

To the Honorable Thomas F. Croake, United States District Judge, Southern District of New York:

The undersigned Referee in Banruptcy, acting as Special Master, pursuant to the order of this Court dated July 31, 1963, respectfully reports to this Court as follows:

By application dated January 17, 1967, Theodore W. Kheel and Raymond J. Scully requested that they be authorized to retain as special counsel the firm of Krusen, Evans and Byrne to defend certain lawsuits.

The application shows that the order appointing the trustees authorized them to defend any proceeding at law or in equity in any State or Federal Court as may be necessary for the protection, maintenance and preservation of the assets of the debtor.

By order dated May 23, 1963, the prosecution of all actions against the debtors was stayed. This injunction

was modified by order dated March 24, 1965 so as to permit prosecution of personal injury actions and claims to final judgment. The enforcement of any such judgment continued to be stayed.

A. H. Bull Steamship Co. is a defendant or a prospective defendant in a number of lawsuits arising out of that corporation's ownership or operation of certain merchant vessels. A. H. Bull & Co., Inc. is a defendant or a prospective defendant as agent for owners and operators. The claims involve personal injury, death, maintenance and cure and unpaid wages.

The instant application seeks authority for the trustees to retain the attorneys of record who have undertaken the defense of the claims.

A problem is presented by reason of the fact that the actions and claims are covered by protection and indemnity insurance over a $1,000 deductible. Some of the claims involve third party complaints against stevedores or other defendants.

The application came on to be heard on March 6, 1967 at which time it was adjourned to March 8, 1967 when a number of persons appeared, including the Office of the United States Attorney for this District through Mr. Robbins, Assistant United States Attorney. The Government voiced its opposition to the application on the ground that potentially the estate might be diminished to the extent of the $1,000 deductible attributable to each of the claims which the trustees sought leave to defend. The Government shows that such an arrangement would violate the priority of the United States in any distribution of the assets of these estates.

It further appears that the attorneys whom the trustees seek to retain are not "disinterested" by reason of their claims against the estates for services which have been rendered. Nevertheless, there is authority for the retention of attorneys who are not disinterested if other factors are present. Bankruptcy Act, Section 157.

However, it was recognized that the real parties in interest in the instant application are the personal injury claimants who had not been given notice of the application.

The hearing was further adjourned to April 3, 1967 at which time the affidavit of Carolinda Waters was received for consideration. The Government, on April 3, 1967, pressed its opposition to the granting of the application for want of justification for the incurring of an indebtedness of up to $1,000 as an expense of administration on behalf of each of the personal injury claimants. The trustees did not submit any authority to justify the action sought to be taken by them. The action is indefinite in nature. According to the affidavit of Miss Waters, in pertinent part:

> ". . . the Trustees are still hopeful that it may be possible to work out some arrangement concerning the $1,000 deductible in order that the defense of the actions will not deplete the assets of the debtors in any way."

A representative of certain of the personal injury claimants stated that attorneys for this class of creditors intended to form a committee so that the interests of this group might be adequately protected.

On the basis of all the foregoing, I respectfully recommend that the application be denied at this time without prejudice to renewal.

I do certify:

1. Application for an Order to Employ Attorneys and Notice of Hearing, dated January 23, 1967;

2. Affidavit of Carolinda Waters, verified April 3, 1967;

3. Notice, dated March 8, 1967 with photocopy of the above-mentioned Application and Notice; and

Referee Ryan's Report

4. Minutes of the hearing of March 6th, March 8th and April 3rd, 1967, separately transmitted.

Dated: New York, N. Y.
April 14, 1967.

Respectfully submitted,

EDWARD J. RYAN
Referee in Bankruptcy